State of Small Business Report 2004

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INTRODUCTION

The state of small business is truly reflective of the state of the American economy overall. This nation's 23 million small businesses are the economic driving force, producing 75 percent of new jobs, accounting for more than half of our GDP, and making up 99 percent of all employers. The health of our small firms is inextricably linked to the health of our economy, and its ability to produce and maintain jobs for our workers.

Since President Bush took office in 2001, he has released a small business agenda (2002), a manufacturing agenda which addressed the needs of small manufacturers (2003), along with a long list of small business-related policy proposals to get the American economy back on track. Even though the economic recession officially ended in early 2002 – almost 2 years ago – a unique situation has gripped the country as job losses persist, causing pessimism about the nation's ability to make a real economic recovery.

In the last three years, the Bush administration has the worst job creation record in our history, second only to President Herbert Hoover during the Great Depression. Approximately 2.2 million private sector jobs have been lost in the last 3 years, and the average length of unemployment is at the highest level in 20 years. The weak labor market actually undermines job prospects for new workers, who have either abandoned their job searches or are faced with low wages that barely keep pace with inflation.

Increasingly apparent is the need to give the small business sector the right tools so it can, in turn, provide the necessary jobs to spur economic development in our local communities. Unfortunately, the policy proposals both outlined and implemented by the Bush administration to help small businesses have failed to receive little attention or action. In fact, President Bush's signature economic renewal policy – three tax cuts in three years – have sunken our nation deeper into debt, and have left our small businesses with limited relief.

Aside from tax relief, there is an array of other challenges confronting small businesses in today's global marketplace. Small business owners, their employees, and their families, are the groups hardest hit by the current health care crisis in this country, accounting for the majority of the uninsured.

Small businesses are also limited in their ability to access capital for start-up and expansion, as the federal budget for small business lending programs remains inadequate, and venture capital is often slow to reach areas that would benefit the most from such investment, including low-income and minority communities.

It is also more difficult for small firms to compete with their large counterparts – from offering employee benefits, including retirement plans, and leveraging technology to gaining access to the federal marketplace, engaging in international trade, and navigating the complex world of government regulations.

And given the positive impact small businesses have on job creation and economic growth, it is more important than ever to provide them with assistance in all of these areas. From a policy perspective, several proposals have been laid out in the Republican-controlled Congress and by the Bush administration to help the small business sector overcome the challenges they face today. Yet they have either remained stalled or have been replaced by other more pressing proposals that lack focus on our nation's entrepreneurial class.

In this latest report, the Democrats on the House Small Business Committee review the current state of small business affairs by taking a closer look at this sector's most critical issues and the legislative proposals in Congress – either passed or pending – that could solve them. In an effort to also assess the landscape of the American economy in general, this report also provides insight into the problems small businesses need addressed before job creation in the U.S. is both steady and strong.

Small businesses in this country must be at the center of any policy debate concerning economic strategies and a plan for better job growth in the future. Since small firms form the backbone of our economy and are an integral component of job promotion, it is evident that a sustained period of economic expansion with a stabilized workforce is out of reach without a strong and vibrant entrepreneurial sector.

SMALL BUSINESSES FACE BARRIERS IN ACCESSING CAPITAL AND FINANCIAL SERVICES

Whether large or small, all businesses need capital to succeed. Whether it is start-up costs, expansion, purchasing and repairing equipment, or even employee costs, there are always new expenses. Small firms need affordable financing in order to remain competitive in the marketplace. Traditionally, small businesses with fewer assets to pledge as collateral, uncertain earnings, and high failure rates have had a more difficult time than larger companies when it comes to securing capital.

While access to capital is of paramount concern to small businesses, they also rely on the nation's banking system to provide them with financial services. In addition to loan products, financial services include both deposit products and merchant services. The lack of access to financial services tailored specifically to meet the needs of small firms leaves them facing higher costs and unattractive terms.

CORE FINANCIAL SERVICES PROGRAMS REMAIN UNDERFUNDED

The administration's budget request for FY 2005 seeks to eliminate and severely restrict the Small Business Administration's (SBA) most important business financing programs. The administration's 7(a) Loan Program proposal eliminates the federal government's contribution by taking the program to a zero credit subsidy rate. By shifting the cost to small businesses, the 7(a) Loan Program will fail to remain a viable option for our nation's entrepreneurs. The administration has also proposed to eliminate the Microloan Program, which last year provided $26.5 million in loans and $15 million in technical assistance to this nation's small firms. The White House's contention that Microloan borrowers can be served through other programs is unrealistic, since it is truly a financing safety net for many U.S. small businesses.

LACK OF ACTION ON SMALL BUSINESS ACCESS TO CAPITAL AND FINANCING PROPOSALS

While policymakers have proposed a multitude of solutions that would increase access to capital for small businesses, these measures have failed to be acted upon by the Republican-controlled Congress. Perhaps most representative of this ambivalence is the inaction on H.R. 2802, the Small Business Reauthorization and Manufacturing Revitalization Act of 2003, a bipartisan measure to expand and streamline SBA's business financing programs, allowing lenders and venture capitalists to do what they do best – get capital into the hands of small businesses.

Republican bickering has also prevented Congress from making important changes to the New Markets Venture Capital (NMVC) Program, which provides the framework for venture capital companies to make investments in low-income areas. Unfortunately, the Bush administration's failure to support this fledgling program has limited its success in serving an area of the economy that would benefit greatly from such investment.

If passed, H.R. 2802 would increase the flow of capital to small businesses located in low-income communities, enabling them to grow and prosper while providing the foundation for future economic development.

The Republican leadership has also stalled legislation that would bolster the venture capital industry. In recent years, venture capital funding has declined from a high of over $28.5 billion in the first quarter of 2001 to just over $4.6 billion in the first quarter of 2004. This decline has greatly limited the ability of small businesses to secure equity financing, forcing them to look to other sources. In an effort to encourage equity investment in small businesses, lawmakers introduced H.R. 739, the Small Business Investment Company Capital Act of 2003. H.R. 739, which has minimal cost to the taxpayer, would provide as much as $500 million per year in new investment to our nation's small business sector. Instead of passing this pro-small business legislation, Republicans chose to pass President Bush's dividend tax cut, which encourages investment in large corporations.

With regard to financial services, a proposal is currently pending that would eliminate Depression-era laws that restrict banks from paying interest on funds held in checking accounts. Small businesses are more likely to use basic checking account services than larger companies, which can often leverage their broader business relationship for more preferential deposit services. The Business Checking Freedom Act of 2003, H.R. 758, which passed the House, addresses this problem by repealing such antiquated laws. The legislation continues to languish as the administration and Congressional leaders continue to place emphasis on other initiatives.

THE NEGATIVE EFFECTS ON SMALL BUSINESS FINANCING

Although the financial services industry has seen great change in the last 20 years, small businesses have yet to fully realize the benefits of this change. In order for small companies to realize them, the SBA's loan and equity programs must be modernized and streamlined, while obsolete banking laws need to be repealed. Today, small businesses continue to be challenged by higher capital costs, unfavorable tax regimes, and less competitive financial services products.

Legislative solutions to these problems exist, but unless the Bush administration and the Republican leadership move on these important initiatives, small businesses will continue to face barriers to their success. Without contributions from small businesses and the jobs they create, the economy will struggle to maintain its recent gains and fail to fully regain its previous strength.

THE FEDERAL MARKETPLACE REMAINS CLOSED TO SMALL BUSINESS

In 2002, the federal marketplace accounted for $235 billion, making it the largest in the world. One of the best ways for a small business to grow is to have the U.S. government as a customer. The flexibility, high quality of products, and low costs of working with small businesses should be a perfect match for federal agencies.

Even though the vast majority of businesses are small, the federal government has not achieved its federally-mandated small business goals over the past several years. This includes an overall small business goal, as well as minority- and women-owned business goals. This failure has cost small businesses almost $40 billion in lost contracting opportunities. Unfortunately, these lost contracts translate directly into jobs that small companies could have generated in local communities.

Last May, the General Accounting Office (GAO) released a report that showed the Federal Procurement Data System (FPDS) administered by the General Services Administration (GSA), where information on contract awards for small businesses is gathered, fails to accurately reflect the number of contracts awarded to small businesses. The report concluded that large businesses were misrepresented – and miscounted – as small ones. This important GAO evaluation calls into question the already tenuous standing of small businesses in the federal marketplace.

REMEDIES TO HELP SMALL BUSINESSES GET THEIR FAIR SHARE OF CONTRACTS

In the fall of 2002, the Bush administration unveiled its plan to increase opportunities for small businesses in the federal marketplace. While the administration acknowledged the harm contract bundling does to small businesses, the plan did little to tackle this growing practice. The president's plan will actually lessen small business protections on federal contracts worth less than $5 million, and also fails to allocate additional resources for real enforcement.

In the 108th Congress, legislation was proposed and passed unanimously out of Committee, H.R. 2802, the Small Business Reauthorization and Manufacturing Revitalization Act of 2003, which will make substantive changes to improve the ability of small firms to access government contracts.

For the past several years, federal government agencies have been intent on contract consolidations – combining work that could be performed by small businesses into mega-contracts. In order to bid on these contracts, small businesses must identify other small firms and pool their resources to perform jobs in numerous industries and in various locations throughout the country.

H.R. 2802 would ensure mega-contracts are reviewed for their potential impact on small businesses. The bill also increases the amount of time that small firms would have to team together and bid on such contracts. Republicans object to these changes on the grounds that competition for contracts would be limited and extending timeframes for bids would be unfair to large corporations. Ironically, by virtue of the size of mega-contracts, competition is limited *only* to large companies.

Giving small businesses the tools they need to be competitive would create an environment that would ultimately lower the costs of contracts to taxpayers. The SBA has such limited resources available that providing assistance to small firms in accessing federal contracts has been virtually non-existent. H.R. 2802 would increase and enhance these resources, giving them a true advocate for increasing their ability to bid on – and win – government prime contracts and subcontracts.

Minority-owned businesses have seen their share of federal procurement diminish over the past several years. From 1995 to 2002, participants in the 8(a) Program – a business development program for minority-owned companies administered by the SBA – have seen their share of contracts drop from 3.84 percent of total federal procurement to 2.39 percent. Rather than supporting changes to this important program, which continues to be the primary vehicle for which minority-owned firms enter the federal marketplace, the administration has done nothing but marginalize it.

THE REALITY OF SMALL BUSINESS AND FEDERAL CONTRACTING

There are a number of obstacles preventing the full participation of small businesses in the federal marketplace. The computer system administered by the government to track actual small business participation in contracting has fallen into disrepair. The administration's plan to increase small business access to contracts was not provided with adequate resources to ensure that it was implemented. Federal agencies continue to rely on large corporations for the vast majority of contracts by exploiting loopholes in provisions designed to increase access of small businesses.

In 2000, a procurement program to assist women entrepreneurs secure contracts was made law, but the Bush administration has refused to implement it. Minority business owners continue to be pushed aside, as programs to assist them are watered down to the point of ineffectiveness. Given these barriers, there is no question that small companies are worse off now with respect to government contracting than they have been in years. As it currently stands, fewer than two percent of U.S. companies receive more than 77 percent of all federal contracts. As this trend continues, competition is practically eliminated and taxpayers will inevitably pay substantially more for goods and services purchased by the U.S. government.

HEALTH CARE: THE NUMBER ONE ISSUE FOR SMALL BUSINESS

In 2003, the Kaiser Family Foundation announced that health care premiums for small businesses rose by double digits for the third consecutive year. The report also indicated that there is little reason to expect costs to plateau in 2004. These increasing costs explain why of the estimated 43 million uninsured Americans, nearly 60 percent either work for a small business or have a family member who does. The rising costs of health care are causing a real and growing crisis in the small business community.

Small businesses and their trade representatives have placed health care reform as their number one concern in 2004. Despite this call for reform, the 108th Congress has seen only minor changes to the way that small businesses can offer health care and has passed no legislation that will effectively combat the rising costs.

HEALTH CARE REFORM MEASURES PROPOSED IN THE 108TH CONGRESS

A bipartisan proposal that has failed to reach the president's desk is Association Health Plan legislation. Association Health Plans – or AHPs – would allow small businesses to band together and use their bargaining power to reduce prices and administrative costs. It would also give small businesses the same type of benefits that corporate America already has in obtaining affordable health care for its employees.

Association Health Plan legislation (H.R. 660, the Small Business Health Fairness Act of 2003) has passed the House twice – first in June, 2003 and again in May, 2004, but is awaiting movement in the Senate. Despite a bipartisan vote, it has not received the same level of support from the administration as the Medicare bill. Even though President Bush has continually expressed concerns about the problems faced by small businesses in the health care market, he has not made the AHP solution a primary part of his overall domestic agenda. Unfortunately, the Committee with jurisdiction in the Senate has yet to hold a hearing on this issue and prospects for movement are dim.

Members of Congress have also been looking at a variety of tax credit options to expand affordable health care to small businesses. However, due to costs and a burgeoning federal deficit, many of these ideas have been put on the backburner. Such proposals would provide small businesses with a tax credit for offering health insurance, particularly to low-income employees – a group that traditionally lacks insurance. This would defray the costs of health insurance for these businesses while allowing them to offer a benefit that is extremely important for employee retention.

In addition, Congress has been examining ways to address the issues facing the self-employed. These entrepreneurs are struggling to afford health care and the tax code has created impediments in their ability to do so. H.R. 1873, the Self-Employed Health Care Affordability Act of 2003, is designed to remedy some of these problems by allowing the self-employed to deduct the costs of health care in calculating payroll taxes, something other small businesses can already do. The budget costs would be fairly minimal and could go a long way in reducing the rising number of uninsured in this country.

The only changes made to existing law were the creation of Health Savings Accounts (HSAs) included as part of the Medicare bill (H.R. 1) passed in 2003. There is concern that these accounts could actually make the health care market worse for small businesses by removing healthy individuals from insured populations and creating adverse selection problems.

SMALL BUSINESSES DESERVE ACCESS TO QUALITY, AFFORDABLE HEALTH CARE

It is clear that health care reform, particularly for small businesses, is not receiving the attention that it deserves. Despite strong support from small business groups for these reforms, there has been little accomplished. Without enactment of legislative solutions, the health care needs of small businesses will continue to grow and correcting the problem will be that much more difficult. There are legislative proposals to help provide small business owners with health care options for themselves and their employees, including AHPs, but these measures remain stalled, much to the detriment of the small business community.

A PENSION SYSTEM FULL OF INEQUALITIES

The one issue that has received scant attention in the 108th Congress is comprehensive pension reform. Quality retirement coverage is an extremely important tool for small businesses to recruit and maintain their workforce. Additionally, small business owners need better options as many of their retirement assets are currently invested in their companies. But small businesses simply cannot afford to sponsor employee retirement plans due to the extremely complex reporting requirements and inequities in the tax code that favor large corporations.

Small businesses likely saw their best opportunity for comprehensive retirement reform in the 2001 tax bill that made a number of changes to pension plans. However, in the end, the Bush administration ignored the needs of small businesses and adopted a one-size-fits-all approach. The 2003 tax bill also failed to provide major pension reform, and as a result, small employers are now confronted with the difficult task of setting up pension plans in a tax structure designed for large corporations. The plans available to small businesses are not only complicated, but also offer few incentives because of lower contribution amounts that can be tax deferred.

THE OUTLOOK FOR PENSION REFORM IS BLEAK

Congress has recognized this problem and has worked in a bipartisan manner to offer concrete solutions in a pension bill (H.R. 1776, the Pension Preservation and Savings Expansion Act of 2003) in the 108th Congress. H.R. 1776 is the best vehicle to correct some of the problems facing small business in offering retirement coverage.

Commonly referred to as Portman Cardin (after its co-sponsors), H.R. 1776 would bring the maximum contribution limits of small business retirement plans in line with those of plans offered by corporate America. The continued disparity in the contribution limits between small and large employer plans has only widened the gap in pension coverage for employees of each. By raising the limits for small business plans, it will encourage small businesses to offer such plans, as owners, their employees and families will be able to put more of their hard earned dollars into a tax-deferred investment vehicle.

Portman Cardin also simplifies some of the rules for small business retirement plans, so they are compliant and not subject to penalties and fines. The hope is that it will reduce the operating costs of managing a retirement plan. While it must be recognized that Portman Cardin does provide some relief, there are other measures that could also help small businesses. For those employers who can afford to set up plans, they must comply with the numerous reporting and testing requirements under ERISA (Employee Retirement Income Security Act). These reporting and testing requirements could be further simplified with special “safe harbor” rules for small businesses.

Another measure that could encourage small business owners to offer plans is to increase their tax credit for the costs of establishing a plan. Despite clear support for this, the 2001 tax bill provided only a $500 credit for three years to defray the costs of setting up a pension plan. Increasing this amount could help encourage small businesses to elect to offer a plan. For example, Congress originally proposed a $6,000 credit for small businesses for the costs associated with implementing a pension plan for its employees. Increasing it to this level would reward both the employer and the employees.

Rather than taking the issue on, the Bush administration has proposed enhanced savings accounts in the last two budgets as its substitute for real pension reform. These savings accounts could actually have the effect of reducing pension coverage for small businesses. If passed into law, they would reduce the incentive for small business owners to offer retirement plans to their employees. Many employers who already offer coverage would likely drop their plans and use these accounts as their only retirement vehicle. The proposals are extremely expensive and could have far reaching consequences for small employers and their employees. Such savings accounts could actually increase the dependence on Social Security benefits as the primary source of retirement income for many individuals.

SMALL BUSINESSES NEED PENSION FIX

It is estimated that less than one-third of employees working for firms with fewer than 25 employees are covered by a retirement plan, and only about half of employees working with firms between 25-99 people are covered. In comparison, over 80 percent of employees working for firms with over 100 employees are covered by a retirement plan. Many small businesses simply cannot afford to sponsor employee benefit plans due to the extremely complex reporting requirements and inequities in the tax code which gives an edge to large corporations.

Reforming our pension system to account for the needs of small businesses must become a priority. When employers offer a plan, it increases savings rates for employees and also offers them a tremendous benefit. There are a number of low-cost measures that could put small businesses on the same playing field as their corporate counterparts by enabling them to offer retirement benefits to their employees.

REGULATIONS AND PAPERWORK WEIGH HEAVILY ON SMALL BUSINESS

By far, the biggest complaint small businesses have about the federal government is the amount of regulations and paperwork imposed on them. Not only is this burden costly and time consuming, but it also puts small businesses at a disadvantage compared to their foreign and domestic competitors. In a large business, the costs of compliance can be spread over an extensive volume of production, yet for small entities, a burdensome regulation could affect the ability to set competitive prices, devise innovations, or even make a profit. In fact, the SBA's Office of Advocacy commissioned a study that found for firms employing fewer than 20 employees, the annual regulatory burden was nearly $6,975 per employee – almost 60 percent higher than firms with over 500 employees.

REGULATORY BURDEN IS INCREASING FOR SMALL FIRMS

When President Bush unveiled his Small Business Agenda in early 2002, streamlining and reducing the regulatory burden were at the top of his list. Yet a recent GAO report revealed that 2002 was a record year for increased paperwork and regulation with agencies producing 80,000 densely packed pages of new rules, notices and advisories. In addition, the GAO report stated that since the Bush administration took office, regulations and legislation have added over 720 million compliance hours per year.

Regulatory compliance and paperwork issues are not new for small business. More than 20 years ago, Congress passed both the Paperwork Reduction Act (PRA) and the Regulatory Flexibility Act (RFA) in an effort to minimize the time spent and costs incurred by small businesses on federal regulations. In 1995, Congress passed the Small Business Enforcement Regulatory Enforcement Act (SBREFA), which has been somewhat effective in holding agencies accountable.

Most recently, in August 2002, the president issued Executive Order 13272 to direct agencies to improve compliance with the RFA. The intent of the Order was to require federal agencies to work more closely with the SBA's Office of Advocacy and properly consider the impact of their proposed regulations on small businesses. Unfortunately, RFA, SBREFA, PRA and EO 13272 are not getting the desired results under the Bush administration.

There are also legislative measures awaiting action in Congress to reduce the regulatory burden on small business. For example, H.R. 205, the National Small Business Regulatory Assistance Act of 2003, which directs the SBA's Small Business Development Centers (SBDCs) to serve as clearinghouses in providing confidential regulatory compliance assistance to small business, is awaiting action in the Senate. There is also legislation pending to strengthen the SBA Office of Advocacy, H.R. 1772, the Small Business Advocacy Improvement Act of 2003, making it more independent from the executive branch and providing it with much-needed resources. Another bipartisan legislative measure, H.R. 1867, the Small Business Paperwork Amnesty Act, would amend the PRA to direct agencies not to impose civil fines for first-time paperwork violations by small businesses.

Just this month, the Small Business Committee held a hearing on the merits of H.R. 2345, the Regulatory Flexibility Improvements Act of 2003, which would define and expand the economic items that must be examined by agencies, setting out requirements for greater precision in performing the analyses. More importantly, this bill increases the responsibilities of the IRS under RFA and applies the panel process to IRS, CMS, and FCC rules that have a significant economic impact on a substantial number of small businesses. An array of different bills aimed at tackling the regulatory issue facing small firms today remain stalled by the Republican-controlled Congress, as the White House continues to issue regulations that disproportionately weigh on our entrepreneurs.

GIVING SMALL BUSINESSES THE RELIEF THEY NEED FROM FEDERAL REGULATIONS

There is a widening gap between large and small businesses and the hours and costs they spend trying to comply with federal regulations. The growing burden weighs most heavily on our small firms, preventing them from expanding and creating jobs. While Republicans may talk about regulatory reduction, the truth is the Bush Administration holds the single year record for the largest increase in the paperwork burden. There are a variety of bipartisan legislative solutions that are currently awaiting action in Congress, but many have been pushed aside as other non-small business related priorities have taken precedence. Since small businesses are the main job creators in this nation, reducing the regulatory burden on them will only help to create employment opportunities and expand economies at the local level.

GROWING COMPLEXITY AND TAX BURDEN ON SMALL BUSINESSES

With continued attention on increased outsourcing and relatively weak job creation, there has been an emphasis on heightening the global competitiveness of small businesses. Congressional leaders have been looking at ways to simplify the tax code and reduce the tax burden on small firms to encourage domestic business growth. Despite bipartisan support to provide comprehensive tax relief to small businesses, there have been relatively few measures enacted in the 108th Congress aimed at them, which will ultimately lead to job creation and economic expansion.

Lawmakers agree that stimulating investment in the small business sector is sound economic policy. The major fiscal tool often used to encourage such growth is through tax code reforms. As part of this effort, measures have been examined that would put small businesses on the same playing field as their large corporate counterparts. With the increasing number of changes in the tax code over the last three years, small businesses are spending increasing amounts of time and resources on compliance, particularly in search of provisions that reward investment.

TAX INITIATIVES PASSED AND FAILED

In the 108th Congress, the major vehicle in which tax reform was available was the 2003 Jobs and Growth Tax Relief Reconciliation Act (H.R. 2). Given this $350 billion tax cut was passed into law, the small business sector saw relatively little benefit in terms of simplification and tax relief. In fact, small businesses on average, received a tax break of less than $500, and instead the legislation focused on providing a dividend tax cut to large corporations. The only targeted small business tax cut measures that were included will expire in the next few years.

At the beginning of this Congress, small businesses were hoping to see a number of their tax issues addressed. They were optimistic that Section 179 equipment expensing would become permanent – a provision in the tax code that allows businesses to immediately write off the costs of a capital purchase. They predicted expansion of bonus depreciation for future years – an important tool to both simplify their recordkeeping and encourage investment. While both of these measures were included in the tax package, they were both sunset to make room for a corporate dividend tax break that accounted for nearly half of the bill's cost. The dividend tax cut not only provides no benefit to small businesses, but also could have the adverse effect of driving investment away from them.

The Jobs and Growth Package also failed to make the expensing and bonus depreciation permanent, and left out any initiatives to simplify the tax code. This one-size-fits-all approach is a major reason that a recent study sponsored by the SBA's Office of Advocacy discovered that tax compliance costs for businesses with fewer than 20 employees was about twice as much as larger companies.

In fact, a 2001 study conducted by the National Small Business United (NSBU, now NSBA) found numerous provisions in the tax code that unfairly discriminate against small businesses. Since this report was issued, the Bush administration has failed to pass any of its recommendations, despite wide recognition that these inequities serve no sound public policy purposes.

The disregarded reforms include simplifying reporting requirements, creating equity in the ability to offer health care, and offering incentives to encourage retirement coverage. Simplifying the tax code and enacting these changes would have a twofold effect – both of which are positive. It would reduce dollars spent on lawyers and accountants, while at the same time making it clear to small business owners that investment back into their enterprise will yield positive results.

Further, the Jobs and Growth Package compounded the problem of the Alternative Minimum Tax (AMT), something that will have an extremely harsh impact on small businesses in the next decade. While the tax bill provided for some marginal rate cuts that affect small business owners, any gains or savings predicted by these are going to be offset by the increasing class of small business owners who will be subject to the AMT. Rather than addressing the issue – with a cost of an estimated $600 billion to fix – the administration's latest tax bill provided for minimal AMT relief. Although there is broad support to address this issue, among both the middle class and small businesses, the 2001 and 2003 tax bills have effectively tied the hands of Congress. The increased budget deficits have limited the ability to adequately address the AMT issue anytime in the near future.

TAX POLICIES TO RECOGNIZE THE ECONOMIC ROLE OF SMALL BUSINESS

Effective tax policies are often measured by their impact on the economy. While it may be somewhat premature to judge the effects of the 2003 tax bill, to date the predicted economic outcomes have fallen short of expectations. On top of the increased tax compliance costs, small business owners are finding the tax code and the changes provide little incentive and few rewards for investing in their ventures.

If Congress and this administration are able to make the connection that failing to account for small businesses in its policies has created weak economic growth, the future may be brighter for this nation's entrepreneurs. It is critical to recognize that tax policy priorities must put small businesses first. When this change occurs and the tax code is not working against small firms, we will see the type of robust expansion and job creation that we have seen in the past.

SMALL BUSINESSES AS TECHNOLOGY PRODUCERS & CONSUMERS

Today, technology is a key component of the business world. Increasingly, small firms are leaders in the high tech sector, and are responsible for the majority of innovations. In addition to developing technological advances, small businesses are also technology consumers. Unfortunately, small firms continue to lag behind their large business counterparts in technology investment.

Barriers include intimidation relative to costs, inability to access – and afford – high-speed Internet access, and lack of a skilled workforce. It has been estimated that small businesses must spend $10,000 for an initial investment in an e-commerce Web site, with annual maintenance and support costs of $2,000. These costs are prohibitively high for many small firms, as opposed to large businesses that can easily absorb such expenditures.

POLICIES AIMED AT SMALL BUSINESSES IN THE TECHNOLOGY ARENA

Congress has not provided any relief to small businesses that face cost burdens in venturing online. H.R. 49, the Internet Tax Nondiscrimination Act, which would place a permanent ban on taxation of Internet access has not been enacted. Additional bills have been introduced to amend the tax code to provide a broadband Internet tax credit (H.R. 768*)*, and to allow the expensing of broadband Internet access expenditures (H.R. 769). H.R. 138, the Rural America Digital Accessibility Act, was introduced in an attempt to bridge the digital divide in rural America, yet Congress has failed to debate any of these measures.

Small technology companies also face unique obstacles. While nearly 40 percent of high tech workers are employed by small businesses, a number of issues remain that need to be addressed to further solidify the role these firms play in the economy. From financing needs and providing sufficient tools to promoting growth, small businesses focused on technology have an array of challenges that preclude them from reaching their full potential.

Financing is vital to the growth of high tech firms. Yet because of their specialized nature, these small companies are less likely to obtain traditional financing. A source of ready financing for them is venture capital, which can give them the capital infusion they need. In the SBA reauthorization bill, H.R. 2802, there is a provision to ensure that small businesses are able to receive venture capital funding – especially those that participate in programs designed to move technology from the drawing board to the marketplace.

A number of important technology initiatives aimed at small businesses have been cut or eliminated in the Bush administration's FY 2005 budget request. These programs include the Advanced Technology Program (ATP) and the Technology Opportunities Program (TOP), and the National Telecommunications and Information Administration (NTIA) within the Department of Commerce, the Department of Education's Community Technology Centers (CTCs), and the Department of Agriculture's Rural Utilities Service Broadband Loan Program and Electric Loan Program. The administration went so far as to eliminate the Rural Outreach Program and the Federal and State Technology Partnership (FAST) program. These funding shortfalls and program eliminations will have a devastating effect on small companies and their ability to use – and produce – technology.

TECHNOLOGY IS KEY TO SMALL BUSINESS GROWTH

Congress has shown little concern for promoting the technological needs of small businesses and small high tech firms. Failure to enact legislation to address the obstacles small companies face in breaking into e-commerce and tapping into new technology initiatives has cost them millions of dollars, as well as new customers. The growth of high tech companies has also been stifled by a lack of Congressional attention to programs that can help them. Cutting or eliminating valuable federal funding for such programs has shown that the administration is not committed to ensuring the nation's preeminence in technology.

AMERICA'S SMALL BUSINESSES: A GROWING FORCE IN INTERNATIONAL TRADE

International business is no longer just for corporate giants such as Lockheed Martin, General Motors and Microsoft, which can easily carry their brands overseas. Today, small businesses are making deeper inroads in the global marketplace, offering their goods and services to different countries around the world.

In fact, over the past decade, the number of small businesses trading overseas has more than tripled. Even with a competitive international environment, small firms are finding ways to infiltrate new markets and communicate with potential customers using technology tools, including the Internet and e-mail. According to the SBA, small and medium-sized businesses represent 97 percent of all U.S. exporters, and firms with fewer than 20 employees make up nearly 70 percent of exporting companies. A way for many small businesses to grow and add employees is by expanding their markets – not just domestically, but internationally as well.

FREE TRADE, NOT NECESSARILY FAIR TRADE FOR SMALL FIRMS

In 2003, President Bush unveiled a six-point plan for sustaining America's economic recovery and spurring job creation. This plan included a section on opening new markets for this nation's small businesses, highlighting the fact that jobs in exporting plants pay higher wages on average, and how one in five factory jobs depends on trade.

Yet the Bush administration requested no funding for what is, perhaps, the most important export assistance program targeted at small companies. U.S. Export Assistance Centers (USEACs) give small companies a one-stop shop that meets all their exporting needs. Located in cities across the country, USEACs provide customized export counseling, trade financial assistance, and technology training for a seamless transition to companies doing business overseas. These centers serve as the primary gateway to export assistance for small businesses, offering information and support to those that want to expand internationally.

Another important trade issue for small businesses that remains stalled by the Republican-led Congress and the White House is the trade sanctions the European Union has threatened without the repeal of the ETI (Extraterritorial Income) regime. Ruled as an "export subsidy" by the World Trade Organization (WTO) FSC/ETI must be replaced by another tax-trade system that is compliant with WTO standards. Currently pending in Congress is a FSC/ETI (Foreign Sales Corporation/Extraterritorial Income) replacement bill, which has drawn criticism for including an array of tax breaks aimed at corporations, seen as "rewards" for those conglomerates that move jobs overseas. It has also been criticized for not doing enough to provide support to our small manufacturers that have lost millions of jobs since President Bush took office in 2001.

This administration has also passed a number of free trade agreements – including Chile, Singapore and Australia – that provide little benefit to the small business community. In the Chile FTA, the administration's nontariff barriers (NTBs) present a problem for small- and medium-sized businesses that rely on trade laws to fight import competition. In addition, the antidumping statues inserted in the agreement can be problematic for small firms that tend to feel the impact of dumping more than their larger counterparts. And according to the International Trade Commission, instead of reducing our $42 billion trade deficit, which weighs on our nation – and our small businesses – this agreement will more than double imports from Chile, driving up the deficit even more.

The Singapore FTA will have a similar negative effect on small businesses, as they will have to more readily compete with imports from this Asian powerhouse that will be duty free, especially in the areas of electronics equipment and other machinery. The U.S. apparel industry will also be hard hit, as many of the tariff and quota protections they had enjoyed will no longer apply. This agreement will most likely heighten competition for small businesses and increase the deficit the U.S. has with Singapore in the machinery and apparel industries.

The small business sector also lost in the administration's negotiations of the Australian FTA, which was pursued in an effort to gain access to Australian markets for U.S. entertainment, telecommunications, and pharmaceutical giants. This FTA will also subject small businesses to more competition, as it removes tariffs on 97 percent of manufacturing exports to the U.S., including a 25 percent tariff on light commercial vehicles. The agreement also phases out tariffs on auto parts, agriculture, and textiles, leaving small- and medium-sized firms struggling to compete in an already tough international business environment. Without a seat at the table during negotiations of these free trade agreements, it is our nation's small businesses that stand the most to lose.

HELPING SMALL BUSINESS SUCCEED IN INTERNATIONAL TRADE

International trade is critical to the economic health of our country – just as small businesses are an integral component of a sustained economic recovery. It has been estimated that for every $1 billion worth of U.S. items exported, close to 40,000 jobs, an additional $2 billion in gross national product (GNP), and $400 million in tax revenue are generated. Yet the Bush administration has pursued a number of free trade policies that actually stand to put our small businesses at a competitive disadvantage. In addition, President Bush continues to eliminate important federal programs that aim at providing export assistance to America's small companies.

If the Bush White House and Congress were really dedicated to helping small businesses grow through international trade, funding for such programs would be adequate, free trade agreements would consider the possible impacts they have on small firms, and an array of legislative measures, including FSC/ETI would include benefits not only to large corporations that ship jobs abroad, but also to small businesses that are have a proven track record of keeping jobs here.

CONCLUSION

It was recently reported that small businesses are falling victim to rising inflation in 2004, including climbing interest rates and gasoline prices. It is this economic indicator, coupled with record-breaking deficits and persistent job losses, which have converged to make a full economic recovery out of reach for the U.S.

Often in such lackluster economic times, it is small businesses that have the power to pull this country out of the doldrums by creating jobs, producing revenue, and helping to expand local economies. In fact, during the 1989-1993 recession, small companies created approximately 3.8 million jobs, outpacing large firms by nearly 500,000 jobs. Small businesses are able to lay the foundation for broad economic expansion and sustained job growth. This was evidenced during the technology boom of the 1990s, as thousands of companies came to life – today, these very same companies employ millions of workers.

Unfortunately, the Bush administration has failed to focus on one of the most basic tenets of American society – entrepreneurship. Instead of cultivating an environment in which small businesses can thrive, this administration has undertaken a number of policy initiatives that have hurt the nation's most important economic sector. The direct result has been an outpouring of jobs overseas, an unemployment rate that is 33 percent higher than when President Bush took office, and millions of workers experiencing pay cuts in the few industries that are gaining jobs. Instead of creating firms and encouraging new ideas, the administration has supported policies that have produced economic stagnation.

The cornerstone of President Bush's economic policies for renewal and job creation has been a series of tax cuts totaling approximately $1.7 trillion, which have sent the budget deficit skyrocketing and provided little relief to small firms. Aside from these tax cuts, the Bush administration has slashed the budget of the agency responsible for small business development in this country, the SBA, and has failed to provide meaningful health or pension reform for small enterprise.

Despite promises by the administration to open up the federal contracting arena and provide regulatory relief to small companies, the government fails to miss its small business goals, and President Bush holds the record for the largest paperwork burden increase in a single year. In the areas of trade and technology, these two important elements of competition remain elusive for many small businesses.

This lack of action on a legislative agenda focused on our entrepreneurs has forced the economy into an uneven recovery with little job growth, long periods of unemployment, climbing deficits, and now rising inflation. Given the inability of the Bush administration and Congress to solve the challenges most important to small businesses, such as access to health care and capital, tax and regulatory relief, and fairness in federal contracting, pensions, trade and technology, the current fragile state of our economy will undoubtedly persist.